IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
ROANOKE DIVISION

IN RE: UNITED HOME HEALTH CARE, INC.	)	
	)	**CASE NO. 05-72094**
Debtor	)	
	)	**CHAPTER 11**

APPLICATION FOR ADMINISTRATIVE EXPENSE
FILED BY FAIRLAWN ENTERPRISES, L.L.C.

MEMORANDUM DECISION

The surprisingly challenging matter before the Court is the Application of Fairlawn Enterprises, L.L.C. ("Fairlawn") for allowance of an administrative expense in this case of certain amounts for "holdover" rent and alleged damages associated with the occupancy and vacating by the Debtor ("United") of certain premises formerly occupied by United and purchased by Fairlawn in September of 2005. These premises had been formerly owned by an affiliate of the Debtor and had been conveyed by it to Valley Bank in full satisfaction of the affiliate's debt to such bank, which then sold it to Fairlawn. At the hearing upon the Application, Fairlawn's claim was reduced to three components: (i) "holdover" rent for the period from October 21, 2005, the date United was obliged to surrender the premises to Fairlawn, thru November 6, 2005, the date such surrender actually occurred; (ii) alleged damages to the premises associated with the removal of a burglar alarm system from the premises by the Debtor's contractor; and (iii) the value of a counter removed from the premises which United claims was a fixture and had become part of the building. For the reasons set out below, the Court will partially grant and partially deny such Application.

FINDINGS OF FACT

United and Wilson Palmer Properties, L.L.C. ("WPP") were affiliated companies in that they were commonly controlled by Elizabeth Wilson Palmer. United had been formed and owned by Ms. Palmer's parents, Mr. and Mrs. Wilson, and she inherited sole ownership of same from them. United was an operating company and WPP was apparently a limited liability holding company organized for the purpose of constructing and owning certain business premises occupied by United under a lease arrangement with WPP. The evidence does not establish whether WPP was also solely owned by Ms. Palmer or whether anyone else, such as her husband, had any ownership interest in it. The construction of these premises was financed for WPP by Valley Bank. When United got in financial difficulty and could not pay its bills, this of course adversely impacted WPP, which ended up deeding the property to Valley Bank in lieu of foreclosure and in full satisfaction of its debt to the bank. At that time United was continuing to use these premises as a debtor-in-possession in the present Chapter 11 bankruptcy case. Fairlawn and United agreed that the latter would continue to use the premises from October 1 thru October 15, 2005 at a rental equivalent to $3,750[1] per month. The parties further agreed that thereafter any continued occupancy after October 15 by United would be on a week-to-week basis at the same rental. As it turned out Fairlawn decided that it wanted United out fairly quickly and gave notice to vacate the premises by October 21, 2005. This was actually the day before United's occupancy was due to end under the week-to-week arrangement agreed to by the

[1] The Stipulation states a figure of $3,500 per month, but counsel for the Debtor acknowledged that the correct figure is $3,750 and that seems to be confirmed by other evidence in the case, including the Debtor's Disclosure Statement filed in this case with its Plan of Reorganization.

parties. In any event, United did not vacate the premises until November 6. During this period of "holding over" Fairlawn seeks to recover rent based on a rental rate of $449.36 per day, determined by utilizing a $11,587.50 per month rent figure contained in a lease which it entered into with another company, plus estimated expenses of electricity, water and real estate taxes, divided by 365 days in a year. Under this new lease agreement Fairlawn was to modify the premises substantially and rent would not begin to be due until the earlier of when the tenant began treating patients or 120 days after all building permits necessary to commence work were received. Mr. Robert Jarrett, Fairlawn's managing member, testified at the hearing that he did not apprise United of the new lease or its terms. The amount sought by Fairlawn for "holdover rent" is $6,028.80, which amount is calculated as follows: $449.36 x 16 days less credit of $1,160.96 for balance of October rent paid in advance at rate of $3,500. United takes the position that it paid rent for the entire month of October and that it is only liable for rent for six days in November at the rate of $125 per day, or a total of $750. The Court finds that United incurred liability for rent for its occupancy after October 15 as follows: October 16 - 31: $2,000 (16 days at $125 per day), November 1 - 6: $750 (6 days at $125 per day). The sum of these amounts is $2,750. Mr. Jarrett acknowledged during cross-examination that the Debtor had paid rent for the entire month of October in the amount of $3,750. One-half of this amount, or $1,875, would be applicable to the period October 16 thru October 31. Giving credit for this amount already paid by United against the rent liability of $2,750 results in a remaining balance due of $875.

Fairlawn next seeks $750.00 for damages alleged to have been done to one of the entrance doors supposedly occasioned by the removal of a burglar alarm system leased by

United at the time it vacated the premises ($700) and for damage to the wall resulting from the removal of the alarm system keypad ($50). Mr. Worth Boone, on behalf of Fairlawn's remodeling contractor, testified about the damage to the wall and the damage to the door, which he specifically and unequivocally attributed to the removal of alarm "sensors" from the door "pivot". Mr. Phillip Bane, who testified on behalf of the Debtor, denied that any damage had been done to the door in question or that any sensors had been removed or that there would have been any reason to remove the old sensors as new ones were installed in the new premises to which the Debtor moved after vacating the premises acquired by Fairlawn. The evidence on this point was considerably less definitive than the Court would have preferred. For example, the testimony did not disclose exactly when it was that Mr. Boone found the door in question to be damaged. Although Mr. Bane testified that he believed the doors to the building were in operating condition at the time United left the premises, it was never clear to the Court's satisfaction that he actually made any inspection of the specific door referenced in Mr. Boone's testimony. Neither did the Debtor call as a witness any individual who had actually been involved in the removal of the alarm system to testify about exactly what was done in that process. On a standard of "clear and convincing" evidence, the Court would have to find against Fairlawn. Based on a preponderance of the evidence standard, however, the Court finds the testimony of Mr. Boone to be somewhat more impressive and persuasive than that of Mr. Bane. The Court doesn't doubt that both of them believed what they testified to, but Mr. Boone's experience as a building contractor and his relative independence from the actual contesting parties together with his demeanor on the stand swung the pendulum of evidence slightly in Fairlawn's favor. Based on that testimony, the Court finds that total damage to the building in

the amount of $750.00 resulted from the removal of the burglar alarm system.

The third component of Fairlawn's claim, and the one which the Court has had the greatest difficulty in resolving, concerns the removal of a counter which rested on a tile floor from the premises when United vacated on November 6. This counter was identical to another counter which rested on carpet and which the Debtor also took with it when it left. This latter counter was not attached in any manner to the floor and Fairlawn by the time of the hearing acknowledged that it had no claim to that one. The counter situated on the tile, however, was rather minimally affixed to the building by caulking around the base of the counter which created a bond with the tile floor underneath. The evidence, including pictures of the location on the tile floor where this counter had been located, establishes that there is no grout between the tiles under this counter's "footprint" although all of the remainder of the tile floor is properly grouted. The parties have stipulated that this counter was installed as follows:

a. 12" by 12" tile had been laid on the concrete floor, but had not been grouted, at the time of the installation of the Counter;
b. The counter was placed on top of the ungrouted tile;
c. The tile was grouted around the Counter, but not underneath its edges; and
d. Caulk was placed around the perimeter of the Counter.

Debtor's Exhibit 1, the construction agreement for the business premises submitted by Commonwealth Builders, Inc. to "Beth Wilson", included "cabinets per plans excluding retail area sales counter" and expressly excluded "cabinetry for retail area". Mr. Bane, who purchased United during the course of this Chapter 11 case from Ms. Palmer and had no affiliation with United at the time the building was constructed, testified that United had no intention to make this counter a fixture to the building. He explained that the counter was caulked to the tile floor to prevent moisture during floor cleaning from getting under the counter

and making it susceptible to damage. Mr. Jarrett, who testified on behalf of Fairlawn, testified that based on his inspection of the property before its purchase, he believed the counters were a part of the building rather than separate personal property of the Debtor. Mr. Bane on behalf of the Debtor of course disputed any such assumption as being reasonable or justified. In response to a question from the Court, he testified that he was pretty sure that both of the cabinets were listed on the Debtor's depreciation schedules and had been included in the Debtor's asset schedules, but wasn't certain of this fact. The Court has examined Schedule B filed in this case and has noted that it contains an entry for "furniture, fixtures and equipment" at its business location having an indicated value of $25,000, but without any itemization of such amount. The Debtor did not call Ms. Palmer as a witness to testify about her intention as a principal of both the building owner and the tenant concerning this counter at the time of its installation in the building or offer any reason why she could not have been called. Mr. Boone testified that the cost of obtaining a similar cabinet to the one removed by the Debtor was $9,979.20, although Fairlawn only requested $9,600 in the Application. Fairlawn did not offer any other evidence as to the value of the counter or how much the value of the building was reduced by its removal, either by the testimony of Mr. Jarrett as the managing member of Fairlawn and owner of the property, or by any real estate appraiser. Mr. Bane testified that the cabinet in question was a "stock" cabinet from a supplier and had not been specially designed or constructed for use in this particular building as contrasted with any other building in which the Debtor might conduct its business. He further testified that the counters had been removed to the Debtor's new place of business and were equally suited for use there as the former location. This testimony was not disputed by any testimony offered on behalf of Fairlawn.

As to this issue as well the evidence offered by the parties proved less than satisfactory to the Court. The evidence offered on Fairlawn's behalf was not clear that it was going to spend the amount testified by Mr. Boone to replace the counter or that the diminution in value of the building from the removal of the counter was equal to the cost of obtaining a new one of similar size and quality. Mr. Boone did testify that the plan was that the counter was to be used as a nurse's station for the new tenant. The Debtor failed to offer in evidence any depreciation schedules documenting its ownership of the counters in its regular books and records and failed to offer in evidence the testimony of Ms. Palmer, who would appear to have been in a position to offer the "best evidence" concerning why the counter was installed on ungrouted tile rather than waiting until after this process had been completed before doing so. The Court is left simply to speculate as to why this occurred. It is not able to give any meaningful weight to Mr. Bane's testimony about the Debtor's intention in view of his own self-interest and lack of involvement when the critical events occurred. Based on the evidence presented to the Court, it finds that the counter in question was not specially made for use in the particular premises constructed for United's use by WPP but for use in the Debtor's business operations wherever they might be conducted. It further finds that the counter placed on the tile floor was affixed to that floor by the use of caulk and that the most reasonable inference arising from the fact that it was installed on top of ungrouted tile is an intention at the time of its installation that it would remain in that specific location for the indefinite future, if not permanently.

CONCLUSIONS OF LAW

This Court has jurisdiction of this proceeding by virtue of the provisions of 28 U.S.C. §§ 1334(a) and 157(a) and the delegation made to this Court by Order from the District Court on July 24, 1984. The determination of claims made against a bankruptcy estate is a "core" bankruptcy matter pursuant to 28 U.S.C. § 157(b)(2)(B).

Statutory authority for the allowance of an administrative expense for post-petition rent for the Debtor's use of Fairlawn's property is provided by 11 U.S.C. § 503(b)(1)(A), which deals with the "actual, necessary costs and expenses of preserving the estate." Fairlawn bears the burden of proof to establish its entitlement to an administrative expense claim against the estate and the proper amount thereof. *In re Merry -Go-Round Enterprises, Inc.*, 180 F.3d 149, 157 (4th Cir. 1999). *See generally* Barry Russell, *Bankruptcy Evidence Manual* § 301.53, at 858-59 (2006 ed.).

> A prima facie case under § 503(b)(1) may be established by evidence that (1) the claim arises from a transaction with the debtor-in-possession; and (2) the goods or services supplied enhanced the ability of the debtor-in-possession's business to function as a going concern. After the movant has established a prima facie case, the burden of producing evidence shifts to the objector; but the burden of persuasion, by a preponderance of the evidence, remains with the movant. . . . Mere allegations, unsupported by evidence, are insufficient to rebut the movant's prima facie case."

Matter of TransAmerican Natural Gas Corp., 978 F.2d 1409, 1416 (5th Cir. 1992).

The Court concludes that the "holdover" rent sought by Fairlawn should be denied, except to the extent of $875 determined in the Findings of Fact portion of this Decision, for the following reasons:

1. Proof of a new lease with a new tenant providing for rent to be paid in the

future after significant remodeling expense had been incurred by the building owner is not satisfactory evidence of the fair market rental value of the premises during the "holdover" period and no other evidence of such rental value of the premises in the existing condition in late October and early November of 2005 was introduced.

2. In the absence of such evidence, the rental rate of $3,750 per month agreed to by the parties at the end of September, 2005 is the best evidence of such value.

3. Fairlawn did not give United any notice concerning the damages it might reasonably incur if the latter failed to vacate the premises when notified to do so. Accordingly, United had no reason to realize that the liability it might incur from breach of its contractual obligation to vacate the premises would be measured by anything other than the rent applicable during the period immediately preceding the date it was obliged to vacate such premises. Furthermore, the parties did not make any agreement concerning the rent which would be due if United failed to vacate the property when expected. The Court concludes that Va. Code § 55-223, which makes a "holdover" tenant responsible to the property owner not only for compensation for use and occupation of the premises, but also "any loss or damage sustained by the lessor because of such failure to surrender possession at the time stipulated", is properly interpreted, in the absence of any definitive Virginia case authority on point, to apply to any loss or damage reasonably within the expectations of both parties on the basis of information possessed by them both, not to "lost opportunity" of which the tenant has not been placed on notice. Such an interpretation is in keeping with the basic principle of contract law limiting recoverable damages resulting from a breach of contract to those within the reasonable expectation of the parties at the time of entering into the contract. *Fairfax County*

Redevelopment & Housing Auth. v. Hurst & Assocs. Consulting Eng'rs, Inc., 343 S.E.2d 294, 296 (Va. 1986); *Morris v. Mosby*, 317 S.E.2d 493, 497 (Va. 1984); 5C *Michie's Jurisprudence* 51, Damages § 13 (1998 Repl. Vol.). For these reasons, the Court concludes that $875 should be allowed to Fairlawn for the unpaid balance of rent during the "holdover" period which ended November 6, 2005.

As to the second component of Fairlawn's claim concerning the alleged damage to the building resulting from the removal of the burglar alarm system, the Court has found that $750 worth of damage resulted from such removal. The Court concludes that the Debtor has the same liability in bankruptcy to an aggrieved party for post-petition transactions as it would have to that same party outside of a bankruptcy proceeding. Accordingly, any such damage resulting from the Debtor's use and occupancy of the premises as a debtor-in-possession is a proper administrative claim against the bankruptcy estate. *See generally Reading Co. v. Brown*, 391 U.S. 471 (1968)(allowing administrative claim for tort claims of adjoining property owners resulting from fire negligently caused by debtor-in-possession). Therefore, the Court concludes that this amount should be allowed as an administrative expense of the estate.

The legal test for determining whether any particular item of personal property has become an improvement to some parcel of realty as to become a fixture has been examined in decisions of the Bankruptcy Court for the Eastern District of Virginia in the cases of *In re Concrete Structures*, 9 B.R. 72 (Bankr. E.D. Va. 1981); *In re Shelton*, 35 B.R. 505 (Bankr. E.D. Va. 1983); and *In re Alterman*, 127 B.R. 356 (Bankr. E.D. Va. 1991). These opinions all cite the opinion of the Supreme Court of Virginia in the case of *Danville Holding Corp. v. Clement*, 16 S.E.2d 345 (Va. 1941), which states the governing legal principles to be as follows:

> In the absence of any specific agreement between the parties as to the character of a chattel placed on the freehold, the three general tests are as follows: (1) Annexation of the chattel to the realty, actual or constructive; (2) its adaptation to the use or purpose to which that part of the realty to which it is connected is appropriated; and (3) the intention of the owner of the chattel to make it a permanent addition to the freehold.
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> While, under the first test, there must be actual or constructive annexation, the method or extent of the annexation carries little weight, except insofar as they relate to the nature of the article, the use to which it is applied and other attending circumstances as indicating the intention of the party making the annexation.
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> The second test – adaptation of the chattel to the use of the property to which is annexed – is entitled to great weight, especially in connection with the element of intention. If the chattel is essential to the purposes for which the building is used or occupied, it will be considered a fixture, although its connection with the realty is such that it may be severed without injury to either.
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> The intention of the party making the annexation is the paramount and controlling consideration. The test of intention is given a broad signification. It does not imply a secret, undisclosed action of the mind of the owner of the property. The intention need not be expressed in words; it may be inferred from the nature of the article affixed, the purpose for which it was affixed, the relationship of the party making the annexation and the structure and mode of annexation.

Id. at 349.

Fairlawn's counsel directs the Court's attention to the principle that when an owner affixes some chattel to his own real property, it is presumed that he does so with the intention of making it a fixture. *See generally Alterman*, 127 B.R. 356; *Shelton*, 35 B.R. 505; *Danville Holding Corp.*, 16 S.E.2d at 349. Fairlawn has not disputed United's assertion that it, rather than WPP, the building owner, purchased the counter and put it in the building. The *Concrete Structures* decision, however, held that the rule establishing a presumption in favor of

finding an intent to annex a structure to the land to which it is affixed when done by an owner of the property is not applicable when such attachment occurs as a result of the actions of a third party. *See Concrete Structures*, 9 B.R. at 74.

> [W]hen a landowner consents to the placing of a building on his land by another, without an express agreement as to whether it shall become a part of the realty or remain the property of the person placing it there, in the absence of any other facts and circumstances tending to show a different intention, an agreement will be implied that the building is to remain the property of the one placing it there.

Id. (citing and quoting from *State v. Ancient Order of United Workmen,* 283 P.2d 461, 468 (Kan. 1955)). *Accord* 35 Am. Jur. 2d 763, Fixtures § 80 (1967). In this case the evidence establishes a close connection between United, WPP and Elizabeth Wilson Palmer, but it does not establish an identity of economic interest among them. In the absence of direct evidence which is satisfactory to the Court concerning Ms. Palmer's intention when the counter in dispute was seated on the ungrouted tile of WPP's building, the Court is left to determine whether a presumption of intent to annex or conversely an intent not to annex is applicable. In the absence of evidence that Ms. Palmer was the sole owner of WPP as well as United or that such entities were treated as one and the same without recognition of their separate legal status, the Court concludes that it ought to employ the presumption that United did not affix the counter to the tile floor with the intent of making it a permanent improvement and fixture to the real property owned by its affiliate, WPP. Such a conclusion seems consistent with the continued status of the second counter which was located on carpet rather than tile as United's personal property as it would seem odd to determine that there was an intent to make one but not both counters fixtures to the building. Further, it recognizes that the burden of proof to establish an administrative

expense rests upon the claimant, rather than it being the trustee's or debtor-in-possession's burden to prove the contrary. Accordingly, any deficiency in the evidence must weigh against the granting of the Application.

CONCLUSION

For the reasons noted above, the Court will allow an administrative expense claim to Fairlawn Enterprises, L.L.C. in the amount of $1,625.00 and will deny the balance of its Application. An order to such effect will be entered contemporaneously with the signing of this Decision.

This 18th day of April, 2006.

William F. Stone, Jr.

UNITED STATES BANKRUPTCY JUDGE